Jim's Perspective…

Nuclear Verdicts and ESG

Last year, a jury in Georgia returned a verdict against defendant Ford Motor Co. in the amount of $1.7 billion. This verdict was the outcome of the punitive damages phase of a three week products liability/wrongful death trial against Ford Motor Co. in Gwinnett County District Court located just northeast of Atlanta. The lawsuit was brought by the two sons of Melvin and Voncile Hill that were killed in April, 2014 in the rollover wreck of their 2002 Ford F-250. The basic punitive damages claim against Ford was that it built pickups with a roof that was dangerously designed and defectively weak, and that Ford's actions in selling the trucks amounted to a wanton disregard for life.

Just based on what I have seen over the last ten years or so, jury verdicts in the United States have risen significantly. The verdict against Ford is what the insurance industry and civil tort defense attorneys refer to as a nuclear verdict. In December, Marsh McLennan reported that the average nuclear verdict has more than tripled between 2015 and 2019, going from $64 million to $214 million. Marsh reports a recent $340 million award in compensatory damages against a large American corporation and another $301 billion verdict against a bar in Texas (the bar was negligent of over-serving alcohol to a customer who then collided with, and killed people in another vehicle while driving after leaving the bar, due to the bar customer's drunk driving, blood alcohol level .263). The median verdict in America has gone up by more than 27% between 2010 and 2019 which is significantly higher than the country's inflation rate during that period. Marsh lists three main factors contributing to higher verdicts and nuclear verdicts.

1. **Change in societal attitudes**. There is increased public mistrust of corporations, and a perception that decisions are made with only profit in mind. It is also believed that many corporations, and their insurers, have deep pockets that allow them to pay the disproportionate jury verdicts that are often intended to bridge the wealth gap with individual plaintiffs. The internet and social media have made it easier to access information, such as CEO salaries, bonuses, and endorsement values, further desensitizing jurors to the dollar values awarded and allowing emotions to play a prominent part in nuclear verdicts.
2. **Litigation tactics**. Plaintiffs' lawyers no longer try to present a sympathetic client. Instead, they emphasize directing the jury to consider health and safety for all Americans. They often portray the defendant as a serial offender. The theme is to shift the jury's focus to penalizing the corporate defendant rather than simply compensating the plaintiff.
3. **Litigation funding**. Today, and I think over the last fifteen to twenty years, there has developed a business strategy in which litigation is funded by experienced investors. This reduces the fear of economic hardship that plaintiffs used to face many years ago. The investors may use data and algorithms to select favorable cases, jurisdictions, judges and jury pools that improve the odds of a nuclear verdict.

The increase in nuclear verdicts obviously has an adverse impact on liability insurance and insurers writing liability insurance. Not only will it increase liability loss costs, but it will

increase direct profit and loss costs of the insurer, if the insured brings a claim against the insurer for negligent failure to settle the claim within policy limits. This claim will also include a claim for an award of punitive damages against the insurer for its reckless refusal to settle in states that allow punitive damages to be awarded in civil tort cases.

A special note about Georgia's punitive damages law. In 1987, the Georgia Legislature passed a tort reform law that capped punitive damages at $250,000. However, that law exempted one type of claim from the punitive damages cap, and that was litigation filed for product liability claims. That is part of the Ford lawsuit. In addition, under the Georgia tort reform law, 75% of an award of punitive damages in a product liability claim goes to the state of Georgia, not the plaintiff. So, in the Ford lawsuit, Georgia collected $1.275 billion. Hooray for the taxpayers of Georgia! Oh, and that would include the lucky jurors! Do you suppose the sophisticated investors funding the litigation against Ford decided to pursue the claim in Georgia because of this unique punitive damages law?

Some of what I have discussed above is fueling the development of a very different underwriting tool in the insurance industry. It is called ESG, and it was first developed in the investment world for asset managers, and financial planners. It involves analyzing a corporation or business in a different way from just looking at whether they are making a profit from what they sell or produce. It involves three pillars of possible risk to a business. These are:

- **Environment**.
- **Society**.
- **Governance**.

The environment pillar relates to climate change. It might involve companies with a carbon emission exposure, but it also involves businesses with an exposure to loss from weather related events or something such as earth quakes.

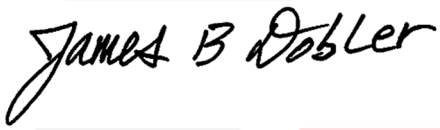
The society pillar involves the human capital of a company and how the company treats customers as viewed from the perspective of the average American. Ford apparently failed the society pillar. It indiscriminately built pickups with awful roofs! This pillar also looks at how a company treats its employees. This includes workforce diversity. It also includes the company's process of developing and managing data privacy. Social risks affect brand image and customer loyalty.

The governance pillar essentially focuses on how the company behaves. What does it give back to the community? After all, it is making a very good profit. It also includes Board structure and diversity, the executive compensation program and accounting practices.

So a third-party agency like Bloomberg uses the ESG process to develop, or calculate, an ESG risk score for a business that perhaps is traded on the N.Y. Stock Exchange. The higher the score, the better the company manages ESG risk. Investors use the ESG score to gauge a company's reputation, stakeholder relationships and risk. I am not sure how underwriters develop, or calculate, an ESG risk score for insurance purposes.

Michael Zuckerman, JD, MBA; Associate Professor of Risk and Insurance Management, Temple University; Fox School of Business and Legal Studies, held a CPCU Zoom meeting about the use of ESG by insurance underwriters. He described this underwriting ESG process as one which focuses generally on "company environment." He mentioned that ESG might be something for brokers and agents to be aware of, and, perhaps review so that they have a better understanding of the client's risk, and have more information on which to make sure the client has proper coverage. He also mentioned that Allianz Insurance Company uses an ESG risk barometer. Zurich is also using ESG. Apparently there are many different ESG programs being used. Many companies simply develop their own program based on factors they have seen other companies use. Zuckerman believes that eventually regulators and trade associations will impact ESG to evolve into a single standard framework of review that will be used generally by the insurance industry.

I just wanted PIA members to be aware of this new underwriting tool, and its use to assess a company's environment and risk exposures. As we all can appreciate, the business of insurance is always experiencing change. Remember when there was no replacement cost coverage for homes?



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